No. 90-1491

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

UNION BANK,
Petitioner,
vs.
HERBERT WOLAS, Chapter 7 Trustee
for the Estate of ZZZZ BEST CO., INC.,
Respondent.

PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

MOTION FOR LEAVE TO FILE BRIEF *AMICUS CURIAE* AND BRIEF OF CALIFORNIA BANKERS ASSOCIATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

MASON C. BROWN
Counsel of Record
ROBERT L. MORRISON
KENNETH N. RUSSAK

PILLSBURY, MADISON & SUTRO

725 South Figueroa Street, Suite 1200
Los Angeles, California 90017
(213) 488-7100

Attorneys for Amicus Curiae
CALIFORNIA BANKERS ASSOCIATION

Lawyers Brief Service / Legal Printers / (213) 383-4457 / (714) 720-1510

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MOTION FOR LEAVE TO FILE BRIEF *AMICUS CURIAE*

The California Bankers Association ("CBA") hereby respectfully moves for leave to file the attached brief *amicus curiae* in this case. The consent of the attorney for the Petitioner has been obtained. The consent of the attorney for the Respondent has been requested but denied.

The CBA, organized as a California nonprofit corporation, is a trade association with over 450 members. CBA's members include virtually every commercial bank in California.

The members of the CBA have a significant stake in the outcome of this case. The effect of the opinion issued below by the United States Court of Appeals for the Ninth Circuit, if not reversed by this Court, would be to eliminate for long-term commercial lenders--and perhaps all commercial lenders--an important defense to bankruptcy preference actions: the so-called "ordinary course of business" exception. 11 U.S.C.§ 547(c)(2)(1979 & Supp. 1991). This exception was first extended to long term lenders by Congress in the Bankruptcy Amendments and Federal Judgeship Act of 1984 when a 45-day limitation on the exception was deleted from the Bankruptcy Code. Since then, the Sixth Circuit has held that the exception is available to creditors under long term consumer instruments, *Gosch v. Burns (In re Finn)*, 909 F.2d 903 (6th Cir. 1990), and the Tenth Circuit has held that the exception is also, at a minimum, available to commercial creditors holding savings certificates which had maturities of up to one year (reserving determination as to whether the exception may be employed by creditors under longer term instruments), *Fidelity Sav. & Invest. Co. v. New Hope Baptist*, 880 F.2d 1172 (10th Cir. 1989). Moreover, the Seventh Circuit based its controversial *Deprizio* decision in part on an assessment that the "ordinary course of business" exception to a preference action is available to long term commercial lenders. *Levit v. Ingersoll Rand Fin. Corp. (In re Deprizio Constr. Co.)*, 874 F.2d 1186 (7th Cir. 1989). Only the Ninth Circuit, the jurisdiction in which CBA members are based, and perhaps the Eleventh Circuit, *Marathon Oil Co. v. Flatau (In re Craig Oil Co.)*, 785 F.2d 1563, 1567 (11th Cir. 1986), have construed the exception to exclude apparently all commercial loans as a matter of law.

The CBA can present a unique perspective on the effect this patchwork quilt of decisions will have on its members, the banking industry and the economy in general. The Petitioner's brief mentions these concerns, but does not fully address the factual, statistical and legislative events germane to the broader industry and national interests at stake. The proposed brief *amicus curiae* examines the importance of the questions presented by the Petitioner in light of issues now receiving intense scrutiny by other branches of the federal government, as well as industry. In part, the attached proposed brief addresses:

(1) The "credit crunch" effect the Ninth Circuit rule will have on credit availability to weakened but viable borrowers;

(2) A projected percentage of loans potentially affected by the Ninth Circuit rule and the impact of the potential liability on banks already challenged by increased credit risks; and

(3) The impact the split in the circuits could have on efforts to improve the efficiency of interstate banking and branching.

Moreover, the Petitioner's brief does not address the Ninth Circuit's apparent exclusion of *all* bank loans from the ordinary course of business exception, not just long term bank loans.

The Petitioner in this case, Union Bank, is a member of the CBA and its Petition for Writ of Certiorari has focused the Court on many important issues raised by the opinion below. The CBA,

however, has a broader industry perspective which the CBA believes will assist this Court in its determination whether to grant certiorari.

Dated: April 23, 1991

Respectfully submitted,

Mason C. Brown
Counsel of Record
Robert L. Morrison
Kenneth N. Russak
PILLSBURY, MADISON & SUTRO

Counsel for *Amicus Curiae*
California Bankers Association

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Mason C. Brown
Counsel of Record
Robert L. Morrison
Kenneth N. Russak
PILLSBURY, MADISON
& SUTRO
725 South Figueroa Street
Suite 1200
Los Angeles, California 90017
(213) 488-7100

Attorneys for California
Bankers Association
as *Amicus Curiae*

INTERESTS OF *AMICUS CURIAE*

The California Bankers Association ("CBA"), organized as a California nonprofit corporation, is a trade association with over 450 members. CBA's members include virtually every commercial bank in California.

The members of the CBA have a significant stake in the outcome of this case. The Ninth Circuit's elimination of the ordinary course of business exception to preference actions for long term loans, and perhaps all bank loans, will adversely affect CBA members. Unless the Ninth Circuit is reversed, CBA members will not be able to defend against bankruptcy preference actions by proving that they dealt with their borrowers on ordinary business terms during the borrowers' unfortunately unsuccessful efforts to avoid bankruptcy. Instead, California banks, and other financial institutions in jurisdictions following the Ninth Circuit, will be given a strong incentive by the Bankruptcy Code to redeploy their loan funds from apparently weakened borrowers to stronger customers. This will significantly limit the ability of banks to work constructively with their troubled borrowers.

SUMMARY OF ARGUMENT

The questions presented by Union Bank's petition are matters of significant national importance. As Union Bank well demonstrates in its Petition for Writ of Certiorari, the decision below not only conflicts with the decisions of three other Circuit Courts of Appeal, it violates principles of statutory construction well established by this Court.

The error below will adversely affect the vast majority of bank loans--perhaps all bank loans--which became the subject of bankruptcy preference actions. The practical consequences of the error will be to increase the loan losses of commercial banks and to tighten credit for their borrowers at the very time at which the federal government and the banking industry are working hard both to make banks safer and to increase the ability of banks to work with their viable, but weakened customers. Moreover, the conflict in the circuits will work at cross purposes with efforts now underway to improve the efficiency and feasibility of interstate banking and branching.

These adverse practical consequences highlight the reasons advanced by Union Bank for granting its petition for writ of certiorari.

ARGUMENT

1. Introduction: The National Context

The decisions of the Ninth Circuit in the case below[1] and its progenitor, *CHG Int'l., Inc. v. Barclays Bank (In re CHG Int'l, Inc.)*, 897 F.2d 1479 (9th Cir. 1990), have come at a time in which the President of the United States,[2] Congress,[3] the Department of the Treasury,[4] the Federal Deposit Insurance Corporation,[5] the Federal Reserve and other federal agencies,[6] as well as private business associations[7] and writers[8] are focusing on two related problems confronting the national banking industry and federal bank insurance funds. On the one hand, recent experience with the thrift industry and a recessionary economy have led to an environment in which banks, reacting in part to what most characterize as "excessive" regulatory criticism,[9] have significantly

[1] *Wolas v. Union Bank (In re ZZZZ Best Co.)* 921 F.2d 968 (9th Cir. 1990).

[2] In his State of the Union Address on January 29, 1991, President George Bush announced a proposal for "[a] banking reform plan to bring America's financial system into the 21st century -- so that our banks remain safe and secure and can continue to make job-creating loans for our factories, business and home-buyers. I do think there has been too much pessimism. Sound banks should be making more sound loans, now." 137 Cong. Rec. S1217 (daily ed. Jan. 29, 1991) (State of the Union Address by President Bush).

[3] Title X of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183, 507-11 (1989) ("FIRREA"), directed various federal agencies to prepare studies of, *inter alia*, federal deposit insurance programs and national banking services.

[4] Pursuant to Title X of FIRREA, *supra* note 3, on February 14, 1991, the U.S. Treasury Department issued its report. *Modernizing the Financial System, U.S. Treasury Department Recommendations for Safer, More Competitive Banks*, Fed. Banking L. Rep. (CCH) No. 1377, Pt. II (Feb. 14, 1991) (hereinafter *Recommendations*).

[5] *See* FDIC, *The FDIC Quarterly Banking Profile*, Fourth Quarter 1990 (1990).

[6] *E.g.*, *Regulators Issue Joint Supervisory Policies*, OCC, FDIC, FRB, OTS Joint Agency News Release (March 1, 1991); Office of the Comptroller of the Currency, *Operations of National Banks*, Quarterly Journal, Vol. 9, No. 4 at 1 (1990) (hereinafter *Operations of National Banks).*

[7] *Credit Crunch: Federal Bank Examination at Cross Purposes*, RTC Rep., Feb 11, 1991.

[8] *E.g.*, *A Message to the Money Men*, U.S. News and World Rep., Apr. 8, 1991 at 70; *The Credit Crunch Is Latest Harsh Blow For Smaller Retailers*, Wall St. J., Apr. 9, 1991, at 1, col. 1.

[9] Michael Boskin, Chairman of President Bush's Council of Economic Advisors, told members of the Senate Budget Committee on February 6, 1991, that "[t]here is enormous evidence that regulation [has] swung too far to the other side." *Brady Says Government May Issue Package to Deal with Credit Crunch in 10*

tightened credit policies. Many, including the President of the United States, have concluded that credit is now too tight, thereby restricting economic growth. The fear, of course, is that well intentioned efforts to improve the capital base of banks and the credit quality of their loan portfolios will exacerbate the current recession and handicap the economy during and after economic recovery.[10]

On the other hand, federal authorities and private analysts have recognized that banks are currently facing greater credit risks than they have in decades. Adding to the problem is an antiquated system of regional banks, fettered from full utilization of existing and developing interstate banking opportunities by statutory and regulatory constraints. Accordingly, although most recognize that the banking

Days, 56 BNA's Banking Rep. (BNA), at 224 (Feb. 11, 1991). Additionally, in a statement accompanying policy guidelines recently issued by the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corp., the Federal Reserve Board, and the Office of Thrift Supervision, the four regulators wrote that some depository institutions may have become overly cautions in their lending practices because of recent credit problems in various sectors of the economy and that "[i]n some instances this caution has been attributed to concerns on the part of lenders that the regulators of depository institutions are applying excessively rigorous examinations standards." *Regulators Release Joint Policy Statement on Various Regulatory, Accounting Issues*, 56 BNA's Banking Rep. (BNA), 394-95 (March 4, 1991). *See also Greenspan Expects Proposals Aimed at Easing Credit Crunch*, Reuters Bus. Rep. (Feb. 20, 1991).

[10] *Bush Reviews Economy, 'Credit Crunch' With Top Advisors, including Greenspan*, 56 BNA's Banking Rep. (BNA), at 124 (Jan. 21, 1991).

industry is fundamentally sound,[11] many are now focusing their efforts on making the industry safer, modernized and more competitive.[12]

The Ninth Circuit's recent rulings (in stark conflict with the positions of three other circuits[13]) that long term lenders cannot enjoy the protection of an important defense against bankruptcy preference actions should be viewed in this context.[14] Indeed, the *ZZZZ Best* decision appears to take the *CHG* holding one step further and, by excluding revolving lines of credit, excludes virtually all commercial loans from the defense.

In *CHG*, the Ninth Circuit held, as a matter of law, that payments on account of long term debt could not be protected by the "ordinary course of business" exception to preference actions provided by 11 U.S.C. § 547(c)(2)(1979 & Supp. 1991). In *ZZZZ Best*, the Ninth Circuit held that even revolving lines of credit are unprotected by the exception. *In re ZZZZ Best*, 921 F.2d at 969 ("We fail to see any significant difference between a revolving line of credit and an ordinary loan for purposes of § 547(c)(2)."). Thus, in the Ninth Circuit's view, the ordinary course of

[11] Board of Governors of the Federal Reserve System, *Monetary Policy Report to Congress* 77 Fed. Res. Bull. 147, 163 (1991) (hereinafter *Report*).

[12] *E.g.*, *Recommendations*, *supra*, note 4.

[13] *Gosch v. Burns (In re Finn)*, 909 F.2d 903 (6th Cir. 1990); *Fidelity Sav. & Invest. Co. v. New Hope Baptist*, 880 F.2d 1172 (10th Cir. 1989); *Levit v. Ingersoll Rand Fin. Corp. (In re Deprizio Constr. Co.)*, 874 F.2d 1186 (7th Cir. 1989).

[14] The CBA will not at this juncture address the merits of the decision below in any detail. Suffice it to say that the CBA generally joins in petitioner's view of the merits of the Ninth Circuit's interpretation of the exception.

business exception affords no protection even to regular, timely payments of interest on a bank revolving line of credit made when the debtor is or could be making additional draws under the line of credit. If, for example, a debtor were to have made an ordinary principal draw on a revolving bank line of credit and then to have made an ordinary payment on the line to the bank, both shortly before bankruptcy, the Ninth Circuit would apparently hold that the exception is not available to the bank. In essence, the Ninth Circuit may have excluded virtually all commercial bank loans from the exception.

Respondent's brief in opposition to the Petition argues that there is no conflict in the circuits. Brief in Opposition of Respondent (hereinafter Respondent's Brief) 11-13. Respondent's Brief, however, fails to discuss the Sixth Circuit's holding in *In re Finn* that "transfers made pursuant to long-term debt [can] be excepted from the avoidance provisions of § 547(b)" under the ordinary course of business exception of § 547(c)(2). *In re Finn*, 909 F.2d at 908. Respondent's discussion of the conflict question likewise ignores the Tenth Circuit's holding in *Fidelity* that obligations with terms of up to one year can enjoy the benefit of the exception. *Fidelity*, 880 F.2d at 1176-77. These decisions starkly conflict with the holdings of the Ninth Circuit that obligations with maturities as short as seven months are not covered by the exception. *In re ZZZZ Best*, 921 F.2d at 969.

Moreover, Respondent casually dismisses as *dicta* the position adopted by the *Deprizio* court that payments on long term debt can be covered by § 547(c)(2). Respondent's Brief 8. Although the rationale of the *Deprizio* decision is complex, the Seventh Circuit's analysis of the applicability of the

ordinary course of business exception played a significant role in its decision. The Court there held that equitable or policy considerations could not defeat the Trustee's position at least in part because long term lenders were protected by § 547(c)(2). *In re Deprizio*, 874 F.2d at 1200 ("In light of these exclusions, there is no reason to use ambulatory arguments of 'equity' or 'policy' to defeat the Trustee's claims in this case."). In the Ninth Circuit, there can be no such reliance.

Whether or not the *Deprizio* court's analysis of the exception was *dicta*, Respondent's Brief only highlights the depth of the conflict in the circuits by suggesting that the Eleventh Circuit has developed a position consistent with the Ninth Circuit rule that the § 547(c)(2) exception "is directed primarily to ordinary trade credit transactions." *Marathon Oil Co. v. Flatau (In re Craig Oil Co.)*, 785 F.2d 1563, 1567. (11th Cir. 1986).

As set forth in more detail below, the net effect limiting the exception to short term trade debt, if not excluding virtually all commercial loans from the exception, will be to tighten credit and to increase loan losses suffered by banks (and other commercial lenders). Moreover, the conflict in the Circuits will needlessly complicate efforts to facilitate existing and developing interstate banking opportunities, as well as to improve the efficiency and competitiveness of our national banking system.

2. Magnitude of the Problem.

The questions presented by Petitioner are issues of significant magnitude both to California banks and to the lending community nationwide. At a minimum,

the Ninth Circuit has clearly excluded long terms loans--if not all bank loans--from protection under § 547(c)(2). Moreover, the Ninth Circuit has adopted a very restrictive definition of short term debt, holding that loans with maturities as short as seven months are not "short term loans." *In re ZZZZ Best*, 921 F.2d at 969.

The percentage of loans potentially affected by these rules is significant.[15] According to data obtained from the Federal Deposit Insurance Corporation's database of Bank Call Reports, commercial banks reported $1.014 trillion of fixed rate[16] loans

[15] There are no data which can support a meaningful estimation of the actual dollar volume of loans potentially affected by the Ninth Circuit rule, in part because no statistics are kept which identify borrowers which are likely to file bankruptcy petitions and in part because no statistics are maintained which compile the number of preference actions filed or threatened in pending bankruptcy cases. Moreover, the nature of the ordinary course of business exception makes it more difficult to identify payments at risk under the Ninth Circuit rule because the exception is by definition primarily available only to creditors which receive payments in an ordinary, regular, timely fashion. (Some courts do, however, recognize that a well established pattern of late payments can also be "ordinary" within the meaning of the exception, if other tests are met.) While a lender could conceivably be alerted to preference risks for borrowers making irregular, late payments, the problem in identifying the risk for current, performing loans is significant, and emphasizes the risk and unfairness of the Ninth Circuit rule.

[16] The FDIC records maturity distribution data for variable rate loans as well, but the data is not meaningful for instant purposes, because the maturity distribution of variable rate loans is based upon the time between interest rate adjustments, not the date the loan matures. (The data is maintained primarily to analyze interest rate sensitivity of bank loan portfolios.) Accordingly, a loan due in 30 years with an interest rate adjustable every month would be classified as a loan with a maturity of from zero to three months.

outstanding as of December 31, 1990, with remaining maturities distributed as shown on Table 1 of the attached Appendix. In sum, loans with maturities of one year or less comprised only 34.54 percent, or $350.1 billion of the $1.014 trillion in outstanding fixed rate loans, with the remaining 65.46 percent, or $663.5 billion of the loans, having maturities of over one year.

The data for California banks are quite similar. As of December 30, 1990, the major California domestic banks and California regional banks which provided data to an independent bank analyst ("Reporting California Banks") reported that, excluding loans with maturities of 24 hours or less, fully 76%, or $73.1 billion, of the $96.2 billion in loans outstanding on December 31, 1990 had remaining maturities in excess of one year.[17]

Indeed, the magnitude of the problem is even greater if, as appears to be the Ninth Circuit's view, a "short term" loan is something significantly less than a seven month loan. On a nationwide basis, at least 79.73 percent, or $808.2 billion, of the fixed rate commercial bank loans at December 31, 1990 had remaining maturities of more than three months, with only 20.27 percent, or $205.4 billion with maturities of three months or less. For the reporting California Banks, 83.34 percent, or $80.2 billion, of the loans at December 31, 1990, had maturities greater than three months, with only 16.66%, or $16 billion of the loans with maturities between 1 day and three months.

Nonetheless, for the sake of completeness, the data are presented in Table 3 of the attached appendix.

[17] *1991 Findley Reports on California Banks*, §§ 2, 3. (See Table 2 of Appendix).

Inasmuch as the distribution of loan maturities to pre-petition debtors most likely reflects the distribution of loan maturities generally, one can safely conclude that the vast majority of loans by commercial banks would adversely be affected in circuits adopting the Ninth Circuit rule. Indeed, on a national basis, the Ninth Circuit's rule would at a minimum deny the availability of the "ordinary course of business" exception to approximately 65 to 80 percent of all loans presently outstanding from commercial banks. In California, the impact would be even greater, with the range of long term loans comprising about 75 to 83 percent of all loans.[18]

This problem is compounded by the controversial indirect preference rule, commonly referred to as the *Deprizio* rule, followed by the Sixth Circuit, *Ray v. City Bank & Trust Co. (In re C-L Cartage Co.)*, 899 F.2d 1490, 1492 (6th Cir. 1990), the Seventh Circuit, *Levit v. Ingersoll Rand Fin. Corp. (In re Deprizio Constr. Co.*, 874 F.2d 1186 (7th Cir. 1989) and the Tenth Circuit, *Manufacturers Hanover Leasing Corp. v. Lowrey (In re Robinson Bros. Drilling, Inc.), 892 F.2d 850 (10th Cir. 1989)* and some lower courts, *Cambridge Meridian Group, Inc. v. Connecticut Nat'l Bank (In re Erin Food Services, Inc.)*, 117 Bankr. 21, 29 (Bankr. D. Mass. 1990), *Billings v. Zions First Nat'l Bank, (In re Granada, Inc.)*, 110 Bankr. 548, 549-50 (Bankr. D. Utah 1990); *In re Installation Services, Inc.*, 101 Bankr. 282, 284 (Bankr. N.D. Ala. 1989).

In those cases, the courts held that the preference period can be as long as one year if the

[18] This figure excludes loans with maturities of 24 hours or less.

lender holds the guarantee of an insider of the debtor.[19] If the *Deprizio* rule remains good law and if the ordinary course of business exception is not available to long term lenders, the magnitude of the problem could be enormous. Banks receiving regular, timely payments on debts guaranteed by insiders could be required to defend against preference actions seeking recovery of up to one year's payments. Left to defending against the *prima facie* case, banks will be at the whim of fact finders dealing with such difficult issues as the borrower's solvency at the time of payment and whether the payment enabled the creditor (or, perhaps, the insider) to obtain more than it would have obtained in a liquidation.

3. The Ninth Circuit Rule Will Give Banks an Incentive To Tighten Credit To Existing and New Borrowers.

The ordinary course of business exception was created to buttress one of the primary purposes of the preference statute: to give creditors an incentive to deal with debtors on ordinary business terms during periods of financial difficulty. *See Coral Petroleum Inc. v. Banque Paribas-London*, 797 F.2d 1351, 1355 (5th Cir. 1986); 4 Collier on Bankruptcy ¶ 547.01 at 547-11 (15th Ed. 1991). By penalizing aggressive creditor action and rewarding cooperative behavior, the exception helps reduce the number of bankruptcies because borrowers are granted access to the capital, goods and services needed to earn their way out of financial difficulty. House Comm. on the Judiciary,

[19] The *Deprizio* court based its holding, in part, on an assessment that the ordinary course of business exception was available to lenders. *Deprizio*, 874 F.2d at 1200.

Bankruptcy Reform Act of 1978, H.R. Rep. No. 595, 95th Cong., 1st Sess. 177-78, *reprinted in* 1978 U.S. Code Cong. & Admin. News 5787, 6138 ("The protection thus afforded the debtor [by the preference section] often enables him to work his way out of a difficult financial situation through cooperation with all his creditors."). *See also Coral Petroleum*, 797 F.2d at 1355 (quoting House Report); 4 Collier on Bankruptcy ¶ 547.01 at 547-11 (15th Ed. 1991).

The exception thus has special relevance in relationships in which the customer may have suffered a down-turn, but appears to be at least marginally viable. If lenders and other creditors continue dealing with a troubled customer on ordinary business terms, the customer's efforts to earn its way out of trouble often succeed and the policy of the ordinary course of business exception is vindicated.

Sometimes, however, despite creditor cooperation and ordinary course dealings, a bankruptcy filing follows within the 90 days after the creditor receives ordinary course payments (or within one year if the bank holds an insider's guarantee) and the debtor, or its trustee, attempts to recover the payments for the benefit of the estate.

The ordinary course of business exception protects the creditor under these circumstances. Because neither the creditor nor the debtor engaged in any unusual action during the debtor's slide into bankruptcy, the creditor is allowed to retain the otherwise preferential payments.

This safe haven is granted because many times the creditor is correct in its assessment that its borrower, although weakened, is viable. If in such

cases a creditor were nonetheless to call a loan or to refuse to extend further credit, a modest retrenchment could turn into a full-scale slide into insolvency. Rather than avoiding bankruptcy, bankruptcy is the result. *See In re Sunup/Sundown, Inc.*, 66 Bankr. 1021, 1022 (Bankr. S.D. Fla 1986) ("The preference section of the bankruptcy code was developed to discourage unusual business delays between the debtor and his creditors while the debtor is financially unstable and close to bankruptcy.").

The ordinary course of business exception thus gives the bank an incentive to continue its relationship with its existing but troubled borrowers, so long as the credit and payment relationship is conducted according to ordinary business terms. That way, the bank is not forced to bear the risk that its assessment of the debtor's viability is incorrect. When the bank is correct, the bankruptcy courts are not involved. When the bank is incorrect, the ordinary course of business exception protects the bank's good efforts nonetheless.

In the absence of an ordinary course of business exception, a bank confronted with an apparently weakened borrower might conduct itself entirely differently. Given the possibility that it might have to disgorge up to one year's timely payments, it might well elect not to rely on its assessment that the borrower is viable. The rational bank might well elect to terminate its relationship and direct its limited resources to other apparently stronger customers. Cut-off from an important source of credit, the once viable customer becomes moribund.

This result is at least as likely for long term bank credit facilities as with other credit relationships. In this era of limited credit availability, a bank left

unprotected by the ordinary course of business exception would have strong reason to call loans from its marginally viable, yet fully performing borrowers and to redeploy those loan funds to healthier customers.

Such strategies, rationally driven by the Ninth Circuit rule, would only exacerbate the "credit crunch" plaguing our economy at the very time in which the federal government and industry are working to free up credit to credit-worthy and, perhaps more importantly, troubled borrowers.[20]

In their March 1, 1991, news release and accompanying policy statement, the Office of the Comptroller of Currency, the Federal Deposit Insurance Corporation, the Federal Reserve Board and the Office of Thrift Supervision discussed the factors causing banks to restrict credit and focused on the need to have banks work with weakened borrowers, not abandon them:

> Recent concerns related to a tightening of credit have focused the agencies' attention on regulatory policies and their effects on institutions' willingness to extend new credit and to work with troubled borrowers.
>
> * * *
>
> Depository institutions have traditionally worked with their borrowers who are experiencing problems. In the current economic environment, it is especially important for institutions to avoid shutting off credit to sound borrowers, especially in sectors of the economy that are experiencing temporary problems.
>
> Consistent with sound banking practices, depository institutions, including those with low capital positions, should work in an appropriate and constructive fashion with borrowers who may be experiencing temporary difficulties.

General Statement, OCC, FDIC, FRB, OTS Joint Agency News Release 2-3 (March 1, 1991).

The Ninth Circuit's rule works at cross purposes with the efforts of the these agencies to ease the credit crunch by creating an incentive for banks to reduce their lending to their existing weak, but viable borrowers, rather than working with those borrowers "in a constructive fashion." Excluding banks from the ordinary course of business exception will decrease the willingness of banks to work with borrowers who are weakened, but making regular timely payments on their loans. The Ninth Circuit's rule will thus only add to the problem of banks being forced by regulatory

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[20] *See, e.g.,Fed May Ease Rates Again If Credit Crunch Does Not Abate, Greenspan Says*, 56 BNA's Banking Rep. (BNA) 16 (Jan. 28, 1991) ("We are looking at other ways to restore a modicum of rational lending when we are dealing with credit-worthy customers. . . We are looking at other strategies to confront the credit crunch. We are pressing this issue as readily as we can."), *U.S. Seeks to Curb Recession by Focusing on the 'Credit Crunch'*, Wall St. J., Feb. 4, 1991, at 1, col. 6 ("[T]he 'credit crunch' has become Public Enemy No. 1 here at home.").

pressure to call loans even from borrowers who are fully and timely performing all loan obligations.

4. The Increased Risk Imposed by the Ninth Circuit Rule Threatens an Already Challenged Banking Industry With Increased Loan Losses.

Most observers agree that banks today are simply in no position to absorb the additional liability that will result from the Ninth Circuit rule. As the FDIC reported to Congress on February 20, 1991, "banks by and large are sound and well capitalized, but concerns about the strength of the industry intensified throughout 1990.[21]

Accordingly, the General Accounting Office and the Congressional Budget Office have each issued reports questioning the financial health of large banks and exploring the implications for the Bank Insurance Fund.[22]

The FDIC's most recent Quarterly Banking Profile reports that during the fourth quarter, 1990, banks reported the lowest quarterly income since the banking industry began reporting quarterly income in 1983, an amount which represented a 50% decline from the fourth quarter, 1989. The FDIC explained the results as follows:

> Higher levels of troubled assets and increased provisions for future losses

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[21] *Report, supra,* note 11 at 163. *See also, U.S. Banks: A Crisis in the Making?* Los Angeles Times, Sunday Apr. 14, 1991, at A1, c1. FDIC Report, *supra*, 77 Fed.Res.Bull. 163.

[22] Report, *supra* note 11, at *id.*

> were the determining factors in banks' poor fourth quarter results. The $11 billion that banks set aside for future domestic credit losses was the highest quarterly amount ever; the previous record was $7.8 billion for the third quarter, 1990. For the full year, total provisions for losses on domestic and foreign operations were $31.7 billion, $670 million more than in 1989. Troubled assets totalled 2.9 percent of all bank assets at the end of 1990. Total assets increased by $5.7 billion in the fourth Quarter but interest-earning assets *fell* by $14.7 billion. . . . The 2.7 percent growth rate for total banking assets in 1990 was the lowest since the 2.0 percent in 1987. For the second consecutive quarter, the proportion of total assets represented by non-current loans and foreclosed real estate set an all time record.

FDIC, *supra* note 5, at 1-2. *See also Operations of National Banks*, *supra* note 6, at p.1.

The ordinary course of business exception would significantly reduce loan losses of national banks if it were interpreted to cover ordinary, timely payments made on account of long-term loans, not to mention short term revolving lines of credit. Again, a precise quantification of the preference loss exposure is impossible but, as discussed above, the magnitude of the risk is significant.

On the merits, this Court might conclude that the Ninth Circuit correctly held that it should ignore

the unambiguous language of the statute and exclude long term and other bank debt from the protections of the § 547(c)(2) exception. The CBA believes the Ninth Circuit erred and urges this Court to accept review and, when the matter is decided on the merits, to reverse. The important point at this juncture is that, however this Court rules, the ruling will have a significant impact on the loan losses suffered by long term lenders at a time when the banking industry is already challenged by a large number of problem loans.

5. The Conflicting Sets of Rules Threatened by the Ninth Circuit's Stance Will Work at Cross Purposes With Efforts Now Underway to Streamline our Banking System.

As Union Bank's petition well points out, there is a clear conflict in the circuits on the issue presented. The Sixth, Seventh and Tenth Circuits have each taken a much more expansive view of the ordinary course of business exception than the Ninth Circuit, and perhaps the Eleventh Circuit. This patchwork quilt of holdings could well have an adverse impact on existing interstate banking operations, as well as on efforts of the federal government and the banking industry to enhance the efficiency and competitiveness of the national banking system.

According to the Treasury Department's recently published recommendations for improving the banking system, the factors which have interfered with banking efficiency and competitiveness include "archaic restrictions on both geographic location and financial activities [which] have constrained banks ability to follow evolving markets, serve customers, and compete effectively." *Recommendations*, *supra* note 4, at 9. The

solution to this problem, according to the Treasury Department, is to eliminate "the artificial restrictions that constrain a bank's ability to make maximum use of its resources and expertise in serving customers." *Id.* at 10. In turn, "[n]ationwide banking and branching will make banks safer through diversification and more efficient through substantially reduced operating costs." *Id.*

The split in the circuits on the question presented, if unremedied, would require those banks which operate in two or more jurisdictions to develop a multiplicity of credit policies and train different groups of credit personnel. This problem will be acute not only within those Circuits which have ruled on the question. It will be as much of a problem--if not more--in jurisdictions in which the Circuit Court of Appeals has not yet ruled. Moreover, those banks which operate only in jurisdictions adopting the Ninth Circuit's holding--such as many of the members of the CBA--will be at an unfair and unwarranted competitive disadvantage to those banks which lend only in jurisdictions which grant § 547(c)(2) protection to commercial lenders.

Regional differences in substantive law, of course, are not uncommon in our federal system and will no doubt continue to vex banks and other lenders competing regionally or nationally. However, a body of national law such as the Bankruptcy Code should not contribute to the problem. It should be capable of uniform and consistent application so that creditors in one region will have the same rights in a problem loan situation as do creditors in other regions. Certainly, the split in the Circuits should not be allowed to hinder continuing efforts to modernize our national banking system.

CONCLUSION

Union Bank's Petition for Writ for Certiorari should be granted.

Dated: April 23, 1991

Respectfully submitted,

Mason C. Brown
Counsel of Record
Robert L. Morrison
Kenneth N. Russak
PILLSBURY, MADISON & SUTRO

Attorneys for *Amicus Curiae*
CALIFORNIA BANKERS' ASSOCIATION

APPENDIX

Table 1: Remaining Maturity Distribution of Commercial Bank Loans, For all Banks, December 31, 1990
Fixed Rate Loans Totalling: $1,013,634,383
(Dollar Amounts in Thousands)

<table>
<tr><td>0-3 Months:
$205,419,843
20.27%</td><td>3-12 Months
$144,704,985
14.28%</td><td>1-5 Years
$423,833,241
41.81%</td><td>Over 5 Years
$239,676,314
23.65%</td></tr>
<tr><td colspan="2">0-12 Months
$350,124,828
34.54%</td><td colspan="2">Over 12 Months
$663,509,555
65.46%</td></tr>
<tr><td>0-3 Months
$205,419,843
20.27%</td><td colspan="3">Over 3 Months
$808,214,540
79.73%</td></tr>
</table>

Source: FDIC Database of Bank Call Reports
Transmitted by Letter Report To Counsel

Chart of Table 1
Nationwide Maturity Distributions

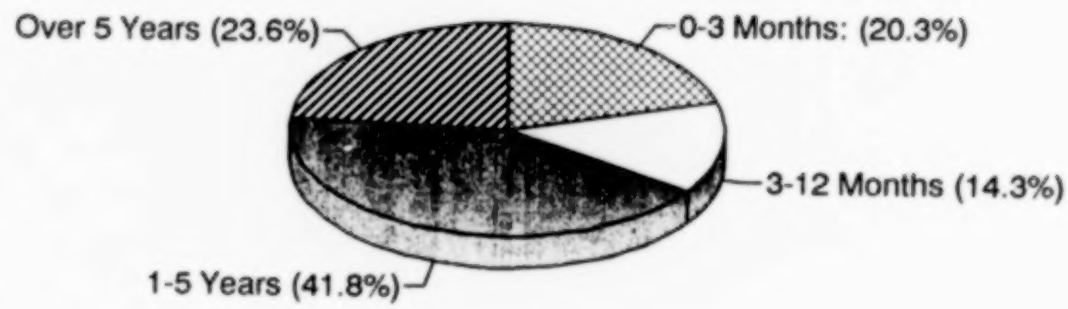

Table 2: Remaining Maturity Distribution of Commercial Loans, for Reporting California Major Domestic and Regional Banks (Excluding Immediate or 1 Day Maturities)
Loans Totalling: $96,204,297
(Dollar amounts in Thousands)

1 Day-3 Months $16,025,858 16.66%	3-12 Months $7,046,594 7.32%	1-5 Years $26,595,914 27.65%	Over 5 Years $46,535,931 48.37%
	1 Day-12 Months $23,072,452 23.98%	Over 12 Months $73,131,845 76.02%	
1 Day-3 Months $16,025,858 16.66%	Over 3 Months $80,178,439 83.34%		

Source: 1991 Findley Reports on California Banks

Chart of Table 2
California Maturity Distributions

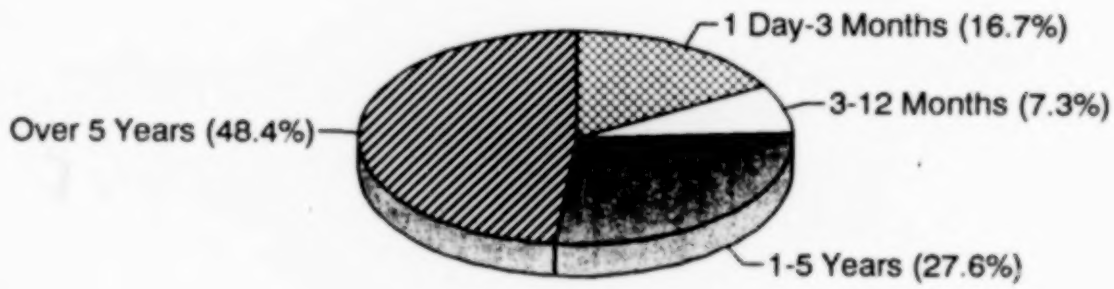

Table 3: Repricing Intervals for Commercial
Bank Loans, For all Banks, December 31, 1990
Variable Rate Loans Totalling: $1,032,126,144
(Dollar Amounts in Thousands)

0-3 Months: $840,957,006 81.48%	3-12 Months $146,565,127 14.20%	1-5 Years $36,971,074 3.58%	Over 5 Years $7,632,937 0.74%
	0-12 Months $987,522,133 95.68%	Over 12 Months $44,604,011 4.32%	
0-3 Months $840,957,006 81.48%	Over 3 Months $191,169,138 18.52%		

Source: FDIC Database of Bank Call Reports
Transmitted by Letter Report To Counsel